No. 11,497

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

JOHN W. PARKER and WELLS FARGO BANK & UNION TRUST CO., as Executors of the Last Will and Testament of J. M. MANNON, JR., Deceased,

Petitioners,

v.

JOSEPH D. NUNAN, JR., COMMISSIONER OF INTERNAL REVENUE,

Respondent.

REPLY BRIEF OF PETITIONERS

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SUBJECT INDEX

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REPLY BRIEF OF PETITIONERS

Respondent's brief is notable in two particulars—(first) it shows that the Commissioner has now substantially abandoned the grounds upon which the Tax Court places its decision and (second) it makes no serious attempt to answer our opening brief. It seems plain that the Commissioner finds it not a little difficult to sustain his contention that the trust income is taxable to the decedent.

Reply to Respondent's Contention That Income From Children's Trusts Was Required to Be Used for Their Support.

The Tax Court held,—as we contended and as the Commissioner himself tacitly conceded before that court, —that the income from the three trusts for the Mannon children was, during the minority of the children, Mrs. Mannon's and not that of the children. On this point the Tax Court said:

> "Petitioners urge and respondent apparently agrees that the children during the minority had no interest whatsoever in the income of the three trusts set up for their benefit. We agree also. The trust instruments and property settlement agreement under which the trusts were set up must, of course, be read together. The property settlement agreement specifies that the trusts were to provide 'for the security' of the wife and that they were accepted by her as satisfactory for 'her' support and maintenance, without mention of the children, emphasizing the lack of legal interest the children had in any of the trust income during their minority." (R. 169)

In other words, the Tax Court made no distinction between the income from Mrs. Mannon's trust and that from the three children's trusts. It was all Mrs. Mannon's. Upon that basis the Tax Court decided that the income from the children's trusts was taxable to the decedent because, so the Tax Court thought, the property agreement

> "surely gave the decedent the *legal** right to *require* the wife first to avail *herself* of the trust income

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*All emphasis throughout this brief, unless otherwise expressly noted, is ours.

before *she* could successfully complain that *her* marital rights of support had been violated." (R. 172)

The Commissioner now contends, however, that the income from the children's trusts is to be differentiated from that of Mrs. Mannon's own trust and that the income of the children's trusts is to be taxed to the decedent because, so it is said, the trusts require Mrs. Mannon to use the income for the support, not of herself, but of the particular child. We quote:

> "We think that a reasonable construction of the trusts for the children is that their mother was required to use the income for the support and maintenance of the particular child, even though she was not required to account to anyone as to how she spent the money." (Resp. Br. 15)

In other words, the Tax Court says that the income is taxable to the decedent because he could have compelled its use to satisfy his obligation to support *Mrs. Mannon,* whereas the Commissioner now says in effect "No, that is not the proper basis for taxing the decedent—the basis should be that he is taxable because he could compel the income to be used to satisfy his obligation to support *the children.*"

Such disagreements and inconsistencies are inevitable when the argument is based (as is the Tax Court's and the Commissioner's) upon implication and assumption and not upon the language of the instruments as written. Neither the Tax Court nor the Commissioner has been able to point to any provision in the trusts or in the property agreement that says that Mrs. Mannon shall use

the trust income for support, either of herself or of the children. They have to *"imply"* that, to get it at all, and they cannot agree even upon what the implication should be.

The Commissioner attempts to find a basis for his implication in the two provisions to which his brief refers—(first) the provision that the income, though given to the particular child, is to be paid to Mrs. Mannon (Resp. Br. 15), which is, of course, making the implication up out of whole cloth, and (second) the provision giving *the trustees* (not the decedent) the right to invade *corpus,* not income, if the immediate income beneficiary should need funds, over and above the trust income, to meet some emergency or to provide for maintenance, support and education (Resp. Br. 16). It is surprising that the Commissioner reverts to this argument that has long been held to be without merit.* It suffices to refer to

> *Suhr v. Commissioner* (C.C.A. 6, 1942) 126 Fed. (2d) 283,

where the husband set up a trust for his wife and her two children and provided that the trustee, in its sole

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*It is to be noted that the Tax Court, although it intimated by way of dictum that it would hold the income of the children's trusts to be taxable to the decedent even if it were to be held that it belonged to the children rather than to Mrs. Mannon (R. 175), did not attempt to support this view by the argument now made by the Commissioner and long since repudiated in the *Suhr* case. The result was again arrived at by the process of implication—the statement being that the emphasis on support in the property agreement "leads to the conclusion that the income was to be used for the children's support and maintenance as included in her own" (R. 175), which is something of an achievement in "implying."

discretion, should have the authority to invade corpus so far as the trustee should

> "deem it necessary to properly care for and support her, taking into consideration such other means of support and sources of income she shall have"

and the Circuit Court of Appeals for the Sixth Circuit answered the very contention that is now made by saying:

> "The decision in Douglas v. Willcuts is not applicable to sustain the present tax. There is nothing in the trust instrument to support an inference that the trust was in discharge of the grantor's legal obligation to support his wife. There was no agreement by her that the benefits of the trust were to relieve him of such obligation, nor was any of the income of the trust used for maintenance or support. *The fact that the grantor, in the exercise of caution, envisioning perhaps the possibility of a change in his fortunes, lodged in his trustee a discretion to invade the corpus of the trust for this purpose, is not enough to warrant a holding that the trust was executed in discharge of the grantor's common law, statutory, or moral obligation to support his wife.*" (p. 285)

Similar provisions for the invasion of corpus at the discretion of the trustee were involved in the following cases, all of which held that, absent any provision that the trust income should be used for maintenance or support, the income was not taxable to the trustor.*

Ralph L. Gray (1938) 38 B.T.A. 584.

Robert P. Scherer (1944) 3 T.C. 776, 798.

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*We might add that even if it were to be held that the income from the children's trusts belonged to the children, though payable to Mrs. Mannon for their account, the rule in California

See, also,

Alex McCutchin (1945) 4 T.C. 1242, 1253, 1254.

Reply to Respondent's Contention That Decedent Could Require Trust Income to Be Used to Discharge His Obligation of Support.

The Commissioner next suggests that in any event, in view of paragraph 2 of the property agreement stating that Mrs. Mannon accepted the conveyance of the family residence, the provision for the payment to her of $700 per month for support and maintenance and the establishment of the trusts as a satisfactory and reasonable provision for her maintenance and support, the decedent could, in his discretion, have compelled the use of the trust income for support and maintenance "simply by refraining from contributing his separate funds to the support of his wife and children" (Resp. Br. 18). Obviously, this is not true unless the decedent had *the legal right* to refuse to furnish support and maintenance. This same argument was made and answered in the *Suhr* case, where the court said:

> ". . . it is argued that under the present agreement, if the grantor should not pay the family expenses, then the wife would be required to use the

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would still be that, without a provision for its use for their support (and no such provision has been pointed to), Mrs. Mannon could not lawfully use it for that purpose so long as the decedent was able to support them (as it is stipulated he was, R. 46), In re Keck (1929) 100 Cal. App. 513, 514; In re Carboni (1941) 46 Cal. App. (2d) 605, 613, and in such a situation the income obviously is not taxable to the trustor. Lillian M. Newman (1943) 1 T.C. 921; Glenn S. Allen, Sr. (1944) T.C. Memo. Docket No. 2149, 3 C.C.H. T.C. Memo. Decisions, Decision No. 13,697 (M); Helvering v. Hormel (C.C.A. 8, 1940) 111 Fed. (2d) 1, affirmed on other grounds in 312 U.S. 552.

trust income for her support and maintenance. This overlooks the fact that the income becomes the sole property of the wife. There is no obligation upon her to support the family if her husband can, and he is not relieved of his legal obligation to do so. It is, of course, true that if he failed, the wife might use her own funds for that purpose, but that would be by her own volition and not through any obligation imposed upon her by the trust." (126 Fed. (2d) at 285)

If the argument of the Commissioner is intended to mean that the decedent did have the legal right to refuse to furnish support because of the property agreement, again the Commissioner is abandoning the decision of the Tax Court and, what is more, is ignoring the applicable California law. As the Tax Court pointed out, in California so long as husband and wife are living together (and it is stipulated that during the taxable years here involved Mr. and Mrs. Mannon were living together, R. 45) they may not, by contract, alter their legal relations except as to their property and the husband cannot limit, much less by contract terminate, his obligation of support. As the Tax Court said:

". . . Although a husband and wife while living together in California may change the status of their property from community to separate property, California Civil Code (Deering) sections 158-160; Siberell v. Siberell, 214 Calif. 767, 770; O'Bryan v. Commissioner, 148 Fed. (2d) 456, they can not while living together validly provide that payment of any certain sum shall discharge the husband's obligation to support and maintain the wife. California Civil Code (Deering) section 159; Brown v.

> Brown, 83 Calif. App. 74, 80-81; Boland v. Boland, 7 Calif. App. (2d) 401, 404. The wife is entitled to support in accordance with the husband's condition and station in life, Shebley v. Peters, 53 Calif. App. 288, and a contract specifying a certain sum for support is bad because it would not, as it should, change with the financial circumstances of the husband. See Garlock v. Garlock, 279 N.Y. 337." (R. 167)

It follows that the decedent did not have the legal right, as the Commissioner would imply, to refuse to meet his obligation of support and thus by indirection force Mrs. Mannon to use the trust income, which he had given to her unrestrictedly, for the purposes of support. Moreover, the whole course of action of the parties themselves under the agreements is inconsistent with the view that the decedent had any such right and utterly at odds with the thought that the decedent had discovered a way, by subterfuge, of reserving an unstated power and control over the trust income.

Obligations and Restrictions May Not Be Added by Implication

The whole difficulty in this case, as indicated above, arises out of the fact that both the Tax Court and the Commissioner seek to *imply* obligations that the written instruments do not contain. The instruments show unmistakably that when the parties meant to deal with maintenance and support they knew how to say so in language that was too clear to be misunderstood. When restriction was intended it was plainly stated. When no restriction or limitation was intended—as was, we sub-

mit, the case with the trust income—none was stated and it does not lie with the Commissioner or the Tax Court to impose by implication restrictions and obligations the parties themselves declined to state. It should not be necessary to support such elementary principles as these by citation of authority, but in view of the lengths to which the Tax Court and the Commissioner have gone in implying things that were not written, it may not be amiss to advert briefly to the statute and case law which must control the decision of this case.

Section 1638 of the California Civil Code provides:

> "*The language of a contract is to govern its interpretation,* if the language is clear and explicit, and does not involve an absurdity."*

In Section 1858 of the Code of Civil Procedure the applicable rule of construction is stated to be:

> "In the construction of a statute or instrument, the office of the judge is simply to ascertain and declare what is in terms or in substance contained therein, *not to insert what has been omitted, or to omit what has been inserted;* and where there are several provisions or particulars, such a construction is, if possible, to be adopted as will give effect to all."*

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*The cases, both state and federal, agree: Cummins v. Bank of America (1941) 17 Cal. (2d) 846, 849 ("*Courts must construe agreements* in their entirety and *as written by the parties, without deletion or interpolation.*"). Bader v. Coale (1941) 48 Cal. App. (2d) 276, 279 (" . . . in interpreting language courts are never justified in searching for subtlety of expression. . . . *the parties are presumed to mean, unless the contrary clearly appears, exactly what they say.*"). Skidmore v. County of Tuolumne (1939) 35 Cal. App. (2d) 525, 531 (" . . . *the courts must take the contract* of the parties *as the parties have written it.*"). Rabbitt v. Union Indemnity Co. (1934) 140 Cal. App. 575, 585 (". . . the *office of the judge is*

If it should be thought that in this case the meaning of the instruments—clear as they are—is in doubt, the settled rule is that they should be construed in the light of the subsequent conduct of the parties under them,* which was entirely out of harmony with any thought that the decedent had the rights which the Tax Court and the Commissioner would imply he contracted for and obtained under paragraph 2 of the property agreement.

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simply to ascertain and declare what is in terms or in substance contained therein, *not to insert what has been omitted or to omit what has been inserted.*"). Loyalton Co. v. California Co. (1913) 22 Cal. App. 75, 77 ("*Where parties have entered into written engagements* which industriously express the obligations which each is to assume, *the court should be reluctant to enlarge them by implication* as to important matters. The presumption is that having expressed some they have expressed all of the conditions by which they intended to be bound."). Sheets v. Seldon (1868) 74 U.S. 416, 423 ("The tendency of modern decisions is not to imply covenants which might and ought to have been expressed, if intended."). Douglass v. Douglass (1874) 88 U.S. 98, 104 ("We cannot interpolate what the contract does not contain. *Our duty is to execute it as we find it, and not to make a new one.*"). Wellsbach Eng. & Management Corp. v. Commissioner, (C.C.A. 3, 1944) 140 Fed. (2d) 584, 587 ("*The court will not* construe a contract in conflict with the plain and accepted meaning of the language used; or *add words to a contract, the meaning of which is clear; or hold a covenantor beyond his undertaking.*"). Henrietta Mills v. Commissioner (C.C.A. 4, 1931) 52 Fed. (2d) 931, 934 ("*The courts will not write contracts for the parties to them* nor construe them other than in accordance with the plain literal meaning of the language used."). Adamson v. Alexander Milburn Co. (C.C.A. 2, 1921) 275 Fed. 148, 153 ("*The courts cannot read into contracts words which the parties did not put there.*"). Sherman v. Commissioner (C.C.A. 9, 1935) 76 Fed. (2d) 810, 811 ("The intention of the parties to a written agreement must be determined from its terms."). To the same effect, Jurs v. Commissioner (C.C.A. 9, 1945) 147 Fed. (2d) 805, 810.

*There are many cases including: Moore v. Wood (1945) 26 Cal. (2d) 621, 629 ("The practical interpretation of a contract by the parties constitutes cogent evidence of intent . . ."). Johnston v. Landucci (1942) 21 Cal. (2d) 63, 71 ("The contemporaneous and practical construction of a contract by the parties is strong evidence as to the meaning of equivocal provisions."). Preston v.

With these elementary principles in mind, we come to their application to the case now before the Court. In our opening brief it was pointed out (pp. 11-12) that there is really no dispute over the rules of *tax* law that are involved. Those rules are simply that if the income of the trusts was Mrs. Mannon's without restriction, limitation or obligation, it was taxable to her, whereas if the decedent had the right, in *his* discretion, to compel the use of the trust income to discharge his obligation or support the income was taxable to him under the rule of

Douglas v. Willcuts (1935) 296 U.S. 1.

These propositions the Commissioner's brief does not controvert nor, in view of the controlling authorities, could they seriously be questioned.

We then undertook an analysis of the trust instruments, the property settlement agreement and the applicable authorities to determine whether, in point of law, the decedent in this case had the right, in his discretion, to control the use of the trust income and to require it to be devoted to the satisfaction of his legal obligation of support. We then had and we now have no difficulty in stating our position, which is based upon the instruments exactly as they are written. As

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Herminghaus (1930) 211 Cal. 1, 11 (". . . such ambiguity has been fully explained by the construction of the contract by the parties themselves . . ."). Brooklyn Life Insurance Company of New York v. Dutcher (1877) 95 U.S. 269, 273 (*"The practical interpretation of an agreement by a party to it is always a consideration of great weight.* The construction of a contract is as much a part of it as anything else. *There is no surer way to find out what the parties meant, than to see what they have done."*). And see in this Court, Holbrook v. Petrol Corp. (C.C.A. 9, 1940) 111 Fed. (2d) 967, 969 and Cutting v. Bryan (C.C.A. 9, 1929) 30 Fed. (2d) 754, 756.

the property agreement makes clear, Mrs. Mannon and the decedent were dividing their properties between them and adjusting all of their property rights upon a broad basis. In this situation it was natural that they should provide for the support and maintenance of Mrs. Mannon and the children and that recognition should be given to Mrs. Mannon's interest in the community property. Accordingly the property agreement provided—and was very express about it—that the decedent would pay $700 a month for the support and maintenance of Mrs. Mannon and the children. Instead of allotting to her a share of the community property, the community property was placed in trust, the income from a half of it (the amount included in Mrs. Mannon's trust) to go to her for life and the income from the other half of it (the amount included in the children's trusts) to go to her during the children's minority. The trust instruments themselves impose no obligation or restriction whatever upon the use of the trust income—much less do they contain any words giving the decedent any discretion or control over its use. The property agreement is likewise absolutely barren of any provision saying how the trust income should be used or giving the decedent any authority over it, though it does state that the entire provision for Mrs. Mannon—the conveyance of the family home, the obligation of the decedent to pay $700 a month for support and maintenance and the establishment of four trusts—was accepted as satisfactory,

reasonable and sufficient provision for Mrs. Mannon's support and maintenance. The Tax Court and the Commissioner would imply from this provision a limitation and restriction upon the use of the trust income and a right in the decedent to control its use that is not to be found in the trust instruments or property agreement. Not only is there no such provision in paragraph 2 of the property agreement, but on this issue we cited authorities where similar and in some instances much stronger language in favor of the Commissioner was held not to give rise to any such limitations or right of control as claimed by the Commissioner. These authorities were manifestly in line with the cases previously referred to holding:

> "Where parties have entered into written engagements which industriously express the obligations which each is to assume, the court should be reluctant to enlarge upon them by implication as to important matters. The presumption is that having expressed some they expressed all of the conditions by which they intended to be bound."

This is particularly so in view of the express provision of the property agreement that

> "This agreement contains the entire understanding of the parties. There are no representations, warranties, promises, covenants, or understandings other than those expressly set forth herein." (R. 56)

Since no limitation upon Mrs. Mannon's use of the trust income was stated and since no provision is to be found giving the decedent discretion or control over the use of the income, it followed that the trust income was not taxable to the decedent.

With all deference, we are constrained to say that the opposing brief makes no serious effort to reply. It is not

said that the cases which we cited do not hold what we said they hold. Only the *Bok* case is mentioned by name and the Commissioner seems satisfied with the attempt of the Tax Court to distinguish that case, although we pointed out in our opening brief (pp. 24-26) that the courts which decided the *Bok* case *expressly* rejected the Tax Court's attempted ground of distinction and placed their decision squarely upon the point stressed by us.

The decisions of the Tax Court which we cited are attempted to be passed off with the statement that the Tax Court distinguished them and, if not distinguishable, our case is the Tax Court's latest decision on the subject. (Resp. Br. 20) In view of the fact that the Tax Court did not intimate that it was overruling or qualifying its earlier decisions, the Commissioner's second ground for disposing of those cases cannot stand. As to the suggestion that they are distinguishable, we believe that this Court will find them helpful analogies on the issue as to the proper construction of the Mannon instruments.

Nor does the Commissioner cite authority to the effect that instruments, such as we have here, are to be construed as giving the trustor the right, in his discretion, to have the trust income used to meet his obligation of support. Indeed, the Commissioner cites only three cases on this phase of the argument and event a cursory reading would make clear that they cannot help the Commissioner's cause. In the first case,

> *Mather v. Commissioner* (1945) 5 T.C. 1001, affirmed *per curiam* 157 Fed. (2d) 680, (C.C.A. 6, 1946) certiorari denied .. U.S. .., 67 S.Ct. 676, 91 L.Ed. (Adv. Ops.) 553,

each of the trusts contained a provision, identical except as to the name of the beneficiary, that

> "The Donor retains the right to elect at any time to have all or any part of the net income used for the maintenance and education of his said son, Rathbun Fuller Mather, or said son's lineal heirs."

Obviously, such a provision gives the trustor the *express* right, in his discretion, to require the trust income to be used for maintenance purposes. Both the Commissioner and the Tax Court have looked long and in vain for any similar provision in the instruments now before the Court.

The next case cited by respondent is

> *Ingraham v. Commissioner* (C.C.A. 9, 1941) 119 Fed. (2d) 223,

which was decided by this Court. In that case the trust instrument itself provided:

> "If at any time during the existence of said trust I, the said Harold Ingraham, shall be lawfully compelled to pay any sum or sums for the support of said Olive Judd Ingraham or of our said children, then the said United States Security Trust Company shall repay to me, the said Harold Ingraham, any sum or sums which I may be thus compelled to pay out of the income of said trust estate."

Here, again, we have an *express* provision in the trust instrument itself that the trustee shall repay to the trustor out of the trust income any amount that the trustor may lawfully be compelled to pay for support. Plainly enough if, as in *Ingraham,* the trust expressly provides that the trustor shall be reimbursed out of the trust income to the

extent that he is required to meet his obligation of support, the trust income is dedicated to satisfy his legal obligation and is therefore taxable to him. There is no similar provision in the instruments now before this Court and the whole opinion in the *Ingraham* case makes it clear that, absent such a provision, the result would have been that the trustor was not taxable.

Nor is there any equivalent provision in the instruments here. We have already answered at pages 7 and 8, *supra,* the Commissioner's contention that under the property agreement the decedent could, as a practical matter, have controlled the use of the trust income by simply refusing to contribute to the support of his wife and children by showing that the property agreement did not, and as a matter of California law could not, give him any such control. Our case is, therefore, within neither the facts nor the principle of the *Ingraham* case.

The last case cited by respondent is

Corliss v. Bowers (1930) 281 U.S. 376,

which, of course, is not even remotely in point. As respondent must know, in that case the trustor was taxed, not because the trust income was dedicated to the discharge of his obligation of support, but because the trust was revocable by him and accordingly he could have had the income for the asking. It is not contended that the Mannon trusts are revocable and if the Commissioner means to suggest that, as was the case in *Corliss v. Bowers,* the trust income here was subject to the trustor's (here, the decedent's) "unfettered command" the answer is simply that that is not so in this case.

The issue before the Court should not be difficult of determination. The controlling question is whether the decedent had the right, in his discretion, to require the trust income to be used in discharge of his legal obligation of support. This is determinable by a reading of the written instruments. The writings themselves are simple enough and the rights and obligations of the parties are clearly expressed. They say that the trust income is Mrs. Mannon's and they do not say that she is to take it subject to any restriction, limitation or obligation nor do they say that the decedent is to have any discretion as to its use. Such provisions, if there are to be any such, can only be supplied by implication and assumption. They are not now there nor has the Commissioner or the Tax Court been able to point to them, though they have suggested that they should be implied. Both statute and case law forbid that they be added in this manner.

Conclusion

It is submitted that under the trusts and property agreement the trust income is given to Mrs. Mannon without any restriction or limitation and without any control over its use, discretionary or otherwise, on the part of the decedent. The Tax Court's determination that the decedent had it within his power to require the trust income to be used in discharge of his legal obligation is not supported by, but is contrary to, the plain language of the instruments. The decision below should

be reversed and the cause remanded with instructions that none of the trust income is taxable to the decedent.

Respectfully submitted,

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